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October 27, 1994

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FEDERAL COMMUNICATIONS COMMISSION  
OFFICE OF SECRETARY

VIA HAND DELIVERY

Mr. William F. Caton  
Acting Secretary  
Federal Communications Commission  
1919 M Street, N.W., Room 222  
Washington, D.C. 20554

Re: Oral Ex Parte Presentation in PP Docket No. 93-253

Dear Mr. Caton:

Pursuant to Section 1.1206(a)(2) of the Commission's Rules, 47 C.F.R. § 1.1206(a)(2)(1993), this is to provide an original and one copy of a notice of an ex parte presentation made on October 27, 1994 by Dave Lasier, Chief Executive Officer of Encompass, Inc., Christopher Dettmar, Vice-President of Encompass, Inc. and Shelley L. Spencer of Swidler & Berlin, Chartered to Jill Luckett, Legal Advisor to Commissioner Rachelle B. Chong. At the meeting, modifications to the competitive bidding rules for designated entities in the entrepreneurial blocks were discussed. The issues addressed included: permitting investment companies to invest in a designated entity's control group, limits on management agreements, resale restrictions, rules for supermajority voting rights, a population based cap on entities bidding in the entrepreneurial block, the need for maintenance of the bidding credits for designated entities, and the need for equalization of the interest rate charged all designated entities.

Copies of materials provided at the meeting are attached.

Sincerely,

  
Shelley L. Spencer

Attachments

cc: Jill Luckett

No. of Copies rec'd 041  
List A B C D E

**STRENGTHENING THE BROADBAND PCS  
COMPETITIVE BIDDING RULES  
FOR DESIGNATED ENTITIES**

The FCC's competitive bidding rules for broadband PCS provide significant opportunities for small businesses to participate in PCS. Several of the requirements, however, are overly restrictive and have the unintended effect of inhibiting the ability of small businesses and other designated entities to raise capital. Other rule provisions, if not clarified, could shift control of a PCS licensee away from the designated entity to a passive investor. If unchanged, these rules will severely restrict the ability of designated entities to participate in PCS.

Based on its experience as a small, entrepreneurial business, Encompass recommends that the FCC modify its broadband PCS competitive bidding rules to:

- 1) permit an "Investment Company," as defined in The Investment Company Act of 1940, including venture capital firms, to invest in a designated entity control group without attribution of the Investment Company's revenues, assets or the personal net worth of its principals;
- 2) specify that super-majority approval by the Board of Directors or shareholders of certain activities is permissible;
- 3) limit management and service agreements to the provision of discrete technical and operational support services and require such agreements to be terminated by the control group upon reasonable notice and without significant financial penalties;
- 4) limit the amount of PCS spectrum any one entity may resell to 25% of the overall capacity of a C&F block PCS system to ensure that use of the spectrum is not indirectly controlled or locked up by a reseller; and
- 5) revise the 10% cap on obtaining PCS licenses in the entrepreneurial blocks to impose a 25 million population-based cap.

## **(1) Funding Designated Entities by Investment Companies**

The FCC's competitive bidding rules for broadband PCS currently require that all members of a bidding entity's control group collectively meet the requirements for qualifying to bid in the entrepreneurial blocks and for qualifying as a designated entity, i.e., a small business or a business owned by minorities or women. For small businesses, such as Encompass, Inc., this rule requires that the aggregate revenues of all members of the control group not exceed \$40 million and that each member of the control group have a personal net worth of less than \$40 million. While well intentioned, the strict requirements of this rule have inhibited the ability of designated entities as a control group to raise capital from traditional funding sources such as venture capital firms. The ability to raise capital at the control group level, not just at the bidding entity level, is proving critical to designated entity participation in PCS.

To address the realistic constraints faced by designated entities and venture capital firms eager to fund designated entities at the control group level, the Commission should modify its rules for control groups to permit "investment companies" to obtain up to a 30% equity and voting interest in the control group without attributing the revenues or assets of the investment company or the personal net worth of any individual investor in the investment company to the control group. (A proposed modified rule is attached as Exhibit A). The exclusion of investment companies from qualification of the control group will permit designated entities to raise the necessary capital to fund the control group while still ensuring that designated entities maintain a controlling interest in the control group. Specifically, Encompass recommends that the FCC:

- (1) adopt the definition of an investment company as defined in Section 80a-3 of The Investment Company Act of 1940, as amended (the "Investment Company Act"), 15 U.S.C. § 80a-3 (1988), without incorporating or adopting the exemptions contained in § 80a-3(c) which, if adopted, would exclude most, if not all, venture capital firms;<sup>1</sup>

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<sup>1</sup> A copy of the relevant portions of the Investment Company Act is attached as Exhibit B. The exemptions contained in § 80a-3(c) include an exemption that removes from the definition of "investment company" any issuer whose outstanding securities are beneficially owned by not more than one hundred persons and which is not making and does not presently propose to make a public offering of its securities. Most, if not all, venture capital firms and funds qualify for this exemption. Accordingly,

(continued...)

(2) impose the same gross revenue cap of \$125 million applied to the entrepreneurial blocks to the gross revenues over the past two calendar years of investment companies who invest in the designated entity control group;

(3) permit investment companies to obtain up to a 30% equity and voting interest in the control group;

(4) require that the members of the control group excluding an investment company or investment companies collectively qualify as a small business or consist entirely of women and minorities; and

(5) maintain the 25% equity requirement for the control group's interest in the bidding entity.

Excluded from the definition of "investment company" are issuers primarily engaged in a business or businesses other than that of investing, reinvesting, owning, holding or trading in securities.<sup>2</sup>

The FCC has incorporated this definition of investment company in the Commission's broadcast multiple ownership rules. See 47 C.F.R. § 73.3555, n.2(c). Incorporation of the definition of an investment company and the exemptions to that definition contained in § 80a-3(b) into the FCC's broadband PCS competitive bidding rules will permit traditional investment sources, such as institutional investors and venture capital funds, to provide a source of capital for designated entities while not permitting unrestricted access to the control group and without eliminating its control.

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<sup>1</sup>(...continued)

inclusion of this exemption from the definition of investment company would prevent venture capital firms from investing in control groups of designated entities.

<sup>2</sup> 15 U.S.C. § 80a-3(b).

## **(2) Super-Majority Voting Requirements**

To attract passive investors a designated entity must be able to provide the passive investor with some degree of representation in decisions of fundamental importance to the bidding entity. Under the current rules, passive investors cannot exercise voting control over an entity bidding in the entrepreneurial blocks because the control group holds 50.1% of the voting control and passive investors are limited to voting interests of 15%. Super-majority voting requirements, however, are not prohibited by the rules and should be expressly authorized by the FCC on matters of fundamental importance to the bidding entity. Super-majority requirements are an important tool for passive investors to feel that they can provide the company some guidance and protect their investment. Encompass requests that the FCC clarify that super-majority requirements are permissible and that the FCC define super-majority requirements as:

votes requiring a majority of the Board of Directors or shareholders of a licensee that together hold not less than 67% of the total voting rights in the bidding entity.

The Commission should further specify that super-majority requirements are permissible on the following matters:

- (1) approval or amendment of any capital contributions and the issuance of shares to satisfy capital contributions;
- (2) reorganization, reclassification or reconstruction of a licensee's share capital;
- (3) amendment of a licensee's dividend policy;
- (4) licensee's initial business plan and initial annual budget and significant modifications thereto.;
- (5) execution of any contract with a commitment of more than 5 years or with a value of more than 20% of the total capitalization of a licensee;
- (6) approval of a capital expenditure or liability of 20% or more of the total capitalization of a licensee;
- (7) a fundamental change in the structure of the licensee, such as liquidation or merger;
- (8) sale of any major asset or substantially all of the assets of a licensee;

(9) acquisition of major assets with a value of \$10 million or more;

(10) execution by a licensee to a third party of any loan documents, guarantees, mortgages, pledges, liens or other encumbrances on a licensee's assets or property for an amount of \$10 million or more and approval of any interest rate attached thereto;

(11) acquisition or sale of any securities of any company including subsidiaries of a licensee;

(12) the offering of shares in a licensee for subscription to the public;

(13) the disposal or transfer of any significant intellectual property rights; and

(14) commencement of any business by a licensee unrelated to PCS.

### **(3) Contours of Permissible Management Agreements**

The FCC's competitive bidding rules permit passive investors to enter into management agreements with entities bidding in the entrepreneurial blocks. The FCC must, however, outline the permissible contours of a management agreement that would prevent a shift in *de facto* control of the applicant.

Encompass proposes that the FCC clarify:

(1) that management agreements will be strictly scrutinized to ensure that they do not transfer *de facto* control of a bidding entity;

(2) that permissible management agreements include a condition that enables the control group to terminate the agreement in its discretion upon reasonable notice; and

(3) that management agreements with significant financial penalties for termination be interpreted as shifting *de facto* control of the applicant.

As the FCC's recently adopted rules on the attribution of spectrum under management agreements provide, management agreements for discrete services, such as technical support, engineering, network design, operation, legal and accounting services, and billing and collection, should be permitted.

#### **(4) Resale Arrangements -- Limited to 25% of Capacity**

One entry strategy being proposed by company's ineligible to bid in the entrepreneurial blocks is to enter into agreements with designated entities to resell a substantial portion, such as 75%, of the PCS spectrum held by a designated entity. In essence, this proposal is an indirect means of capturing spectrum and limiting competition. In addition, these type of resale arrangements with designated entities raise concerns about whether the entity reselling a large portion of the capacity of a PCS license is able to control the designated entity through its purchasing power.

To guard against these anti-competitive practices, Encompass proposes that resale arrangements with a PCS licensee in the entrepreneurial blocks be limited to 25% of its overall capacity during the first five years of the license.

#### **(5) Population-Based Restriction -- 25 Million**

Encompass proposes that the cap on the number of entrepreneurial block licenses held by a single entity be based upon population rather than the number of licenses. Under the FCC's current rules, an entity may hold up to 98 licenses in frequency blocks C and F (10% of the total amount of licenses). A single entity could therefore hold licenses that serve more than 150 million people based upon the population in the top 98 BTA markets, an amount that will far exceed the financial resources of most entities bidding in the entrepreneurial block. Based on its recent modeling and analysis, Encompass has refined its position on the appropriate population based cap for bidders in the entrepreneurial block. Encompass proposes that the Commission adopt a 25 million population-based cap on the number of entrepreneur block licenses held by a single entity. By adopting a population cap, instead of a license cap, all qualified designated entities will have an opportunity to compete in the provisioning of broadband PCS. This population threshold of 10% also will ensure a diversity of designated entities in the entrepreneurial blocks.

## EXHIBIT A

### PROPOSED MODIFIED RULE

An investment company, as defined in 15 U.S.C. § 80a-3(a) and (b), and without reference to or incorporation of the exemptions set forth in 15 U.S.C. § 80a-3(c), shall be eligible to invest in the control group of an entity bidding in the entrepreneur's blocks without its revenues or assets or the personal net worth of its investors being attributable to the control group provided:

- (1) that the aggregate equity and voting interests of any investment companies in the control group do not exceed 30% of the equity and voting interest of the control group;
- (2) that the annual gross revenues of the investment companies for the last two calendar years do not exceed \$125 million; and
- (3) the members of the control group, other than the investment companies, collectively qualify as a small business or are all women and/or minorities.



5TH SECTION of Level 1 printed in FULL format.

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\*\*\* THIS SECTION IS CURRENT THROUGH P.L. 103-262, APPROVED 5/31/94 \*\*\*

TITLE 15. COMMERCE AND TRADE  
CHAPTER 2D. INVESTMENT COMPANIES AND ADVISORS  
INVESTMENT COMPANIES

15 USCS § 80a-3 (1994)

§ 80a-3. Definition of investment company

(a) Definitions. When used in this title, "investment company" means any issuer which--

(1) is or holds itself out as being engaged primarily, or proposes to engage primarily, in the business of investing, reinvesting, or trading in securities;

(2) is engaged or proposes to engage in the business of issuing face-amount certificates of the installment type, or has been engaged in such business and has any such certificate outstanding; or

(3) is engaged or proposes to engage in the business of investing, reinvesting, owning, holding, or trading in securities, and owns or proposes to acquire investment securities having a value exceeding 40 percentum of the value of such issuer's total assets (exclusive of Government securities and cash items) on an unconsolidated basis.

As used in this section, "investment securities" includes all securities except (A) Government securities, (B) securities issued by employees' securities companies, and (C) securities issued by majority-owned subsidiaries of the owner which are not investment companies.

(b) Exemption from provisions. Notwithstanding paragraph (3) of subsection (a), none of the following persons is an investment company within the meaning of this title:

(1) Any issuer primarily engaged, directly or through a wholly-owned subsidiary or subsidiaries, in a business or businesses other than that of investing, reinvesting, owning, holding, or trading in securities.

(2) Any issuer which the Commission, upon application by such issuer, finds and by order declares to be primarily engaged in a business or businesses other than that of investing, reinvesting, owning, holding, or trading in securities either directly or (A) through majority-owned subsidiaries or (B) through controlled companies conducting similar types of businesses. The filing of an application under this paragraph in good faith by an issuer other than a registered investment company shall exempt the applicant for a period of sixty days from all provisions of this title applicable to investment companies as such. For cause shown, the Commission by order may extend such period of exemption for an additional period or periods. Whenever the Commission, upon its

own motion or upon application, finds that the circumstances which gave rise to the issuance of an order granting an application under this paragraph no longer exist, the Commission shall by order revoke such order.

§

(3) Any issuer all the outstanding securities of which (other than short-term paper and directors' qualifying shares) are directly or indirectly owned by a company excepted from the definition of investment company by paragraph (1) or (2) of this subsection.

(c) Further exemptions. Notwithstanding subsection (a), none of the following persons is an investment company within the meaning of this title:

(1) Any issuer whose outstanding securities (other than short-term paper) are beneficially owned by not more than one hundred persons and which is not making and does not presently propose to make a public offering of its securities. For purposes of this paragraph:

(A) Beneficial ownership by a company shall be deemed to be beneficial ownership by one person, except that, if the company owns 10 per centum or more of the outstanding voting securities of the issuer, the beneficial ownership shall be deemed to be that of the holders of such company's outstanding securities (other than short-term paper) unless, as of the date of the most recent acquisition by such company of securities of that issuer, the value of all securities owned by such company of all issuers which are or would, but for the exception set forth in this subparagraph, be excluded from the definition of investment company solely by this paragraph, does not exceed 10 per centum of the value of the company's total assets. Such issuer nonetheless is deemed to be an investment company for purposes of section 12(d)(1) [15 USCS § 80a-12(d)(1)].

(B) Beneficial ownership by any person who acquires securities or interests in securities of an issuer described in the first sentence of this paragraph shall be deemed to be beneficial ownership by the person from whom such transfer was made, pursuant to such rules and regulations as the Commission shall prescribe as necessary or appropriate in the public interest and consistent with the protection of investors and the purposes fairly intended by the policy and provisions of this title, where the transfer was caused by legal separation, divorce, death, or other involuntary event.

(2) Any person primarily engaged in the business of underwriting and distributing securities issued by other persons, selling securities to customers, and acting as broker, or any one or more of such activities, whose gross income normally is derived principally from such business and related activities.

(3) Any bank or insurance company; any savings and loan association, building and loan association, cooperative bank, homestead association, or similar institution, or any receiver, conservator, liquidator, liquidating agent, or similar official or person thereof or therefor; or any common trust fund or similar fund maintained by a bank exclusively for the collective investment and reinvestment of moneys contributed thereto by the bank in its capacity as a trustee, executor, administrator, or guardian.

(4) Any person substantially all of whose business is confined to making small loans, industrial banking, or similar businesses.

(5) Any person who is not engaged in the business of issuing redeemable securities, face-amount certificates of the installment type or periodic payment plan certificates, and who is primarily engaged in one or more of the following businesses: (A) Purchasing or otherwise acquiring notes, drafts, acceptances, open accounts receivable, and other obligations representing part or all of the sales price of merchandise, insurance, and services; (B) making loans to manufacturers, wholesalers, and retailers of, and to prospective purchasers of, specified merchandise, insurance, and services; and (C) purchasing or otherwise acquiring mortgages and other liens on and interest in real estate.

(6) Any company primarily engaged, directly or through majority-owned subsidiaries, in one or more of the businesses described in paragraphs (3), (4), and (5), or in one or more of such businesses (from which not less than 25 per centum of such company's gross income during its last fiscal year was derived) together with an additional business or businesses other than investing, reinvesting, owning, holding, or trading in securities.

(7) Reserved.

(8) Any company subject to regulation under the Public Utility Holding Company Act of 1935.

(9) Any person substantially all of whose business consists of owning or holding oil, gas, or other mineral royalties or leases, or fractional interests therein, or certificates of interest or participation in or investment contracts relative to such royalties, leases, or fractional interests.

(10) Any company organized and operated exclusively for religious, educational, benevolent, fraternal, charitable, or reformatory purposes, no part of the net earnings of which inures to the benefit of any private shareholder or individual.

(11) Any employee's stock bonus, pension, or profit-sharing trust which meets the requirements for qualification under section 401 of the Internal Revenue Code of 1986 [26 USCS § 401]; or any governmental plan described in section 3(a)(2)(C) of the Securities Act of 1933 [15 USCS § 77c(a)(2)(C)]; or any collective trust fund maintained by a bank consisting solely of assets of such trusts or governmental plans, or both; or any separate account the assets of which are derived solely from (A) contributions under pension or profit-sharing plans which meet the requirements of section 401 of the Internal Revenue Code of 1986 [26 USCS § 401] or the requirements for deduction of the employer's contribution under section 404(a)(2) of such Code [26 USCS § 404(a)(2)], (B) contributions under governmental plans in connection with which interests, participations, or securities are exempted from the registration provisions of section 5 of the Securities Act of 1933 [15 USCS §§ 77e] by section 3(a)(2)(C) of such Act [15 USCS § 77c(a)(2)(C)], and (C) advances made by an insurance company in connection with the operation of such separate account.

(12) Any voting trust the assets of which consist exclusively of securities of a single issuer which is not an investment company.

(13) Any security holders' protective committee or similar issuer having outstanding and issuing no securities other than certificates of deposit and

short-term paper.

HISTORY: (Aug. 22, 1940, ch 686, Title I, § 3, 54 Stat. 797; Oct. 21, 1942, ch 619, Title I, Part I, § 162(e), 56 Stat. 867; July 1, 1966, P.L. 89-485, § 13(i), 80 Stat. 243; Dec. 14, 1970, P.L. 91-547, § 3(a), (b), 84 Stat. 1414, 1415; Feb 5, 1976, P.L. 94-210, Title III, § 308(c), 90 Stat 57; Oct. 21, §1980, P.L. 96-477, Title I, § 102, Title VII, § 703, 94 Stat. 2276, 2295.)

(As amended Dec. 4, 1987, P.L. 100-181, Title VI, §§ 604-606, 101 Stat. 1260.)

#### HISTORY; ANCILLARY LAWS AND DIRECTIVES

#### REFERENCES IN TEXT:

"This title", referred to in this section, is Title I of Act Aug. 22, 1940, ch 686, 54 Stat. 789, which appears generally as 15 USCS §§ 80a-1 et seq. For full classification of this Title, consult USCS Tables volumes.

"The effective date of the Revenue Act of 1936", referred to in this section, is probably intended to be a reference to the date of enactment of Act June 22, 1936, ch 690, 49 Stat. 1756, which was enacted June 22, 1936.

"Section 214 of the Interstate Commerce Act", referred to in this section, is § 214 of Act Feb. 4, 1887, ch 104, 24 Stat. 379, which formerly appeared as 49 USCS § 314, prior to the enactment of Title 49 into positive law by Act Oct. 17, 1978, P.L. 95-473, § 3(b), 92 Stat. 1466; similar provisions now appear as 49 USCS § 11302.

"The Public Utility Holding Company Act of 1935", referred to in this section, is Act Aug. 26, 1935, ch 687, Title I, 49 Stat. 838, which appears generally as 15 USCS §§ 79 et seq. For full classification of this Act, consult USCS Tables volumes.

#### EFFECTIVE DATE OF SECTION:

For the effective date of this section, see Act Aug. 22, 1940, ch 686, Title I, § 53, 54 Stat. 847, which appears as 15 USCS § 80a-52.

#### AMENDMENTS:

1942. Act Oct 21, 1942, in subsec. (c)(13), inserted "as amended".

1966. Act July 1, 1966, in subsec. (c), deleted para. (4) which read: "Any holding company affiliate, as defined in the Banking Act of 1933, which is under the supervision of the Board of Governors of the Federal Reserve System by reason of the fact that such holding company affiliate holds a general voting permit issued to it by such Board prior to January 1, 1940; and any holding company affiliate which is under such supervision by reason of the fact that it holds a general voting permit thereafter issued to it by the Board of Governors and which is determined by such Board to be primarily engaged directly or indirectly, in the business of holding the stock of, and managing or controlling, banks, banking associations, savings banks, or trust companies. The Commission shall be given appropriate notice prior to any such determination and shall be entitled to be heard. The definition of the term 'control' in section 2(a) shall not apply to this paragraph.".

1970. Act Dec. 14, 1970 (effective upon enactment on 12/14/70, as provided by § 30 of such Act, which appears as 15 USCS § 80a-52 note), in subsec. (b)(2), inserted "in good faith"; and in subsec. (c), in introductory para., substituted "Notwithstanding subsection (a), none of the following persons is an investment company within the meaning of this title:" for "Notwithstanding subsections (a) and (b), none of the following persons is an investment company within the

# Investment Company in Control Group

*Control Group needs development and bidding funds to participate in auctions.*

- ◆ Investment Company must meet the definition defined in Investment Company Act of 1940. 15 U.S.C. § 80a - 3 (1988), without incorporating or adopting the exemptions contained in § 80a - 3 (c).
- ◆ Limit Investment Company to < 30% ownership and voting.
- ◆ Limit Investment Company to < \$125 Million annual Revenues.

# Management & Service Contracts in Designated Entity Control Group

- ◆ Should not be permitted if they violate the *de facto* control intent of the FCC Designated Entity Control Group Rules.
- ◆ Designated Entity Control Group must have the ability to terminate any management or service contract at its sole discretion given reasonable notice.
- ◆ Any contract with a passive investor in the Designated Entity that has significant financial penalty if terminated by the Control Group, could be construed as *de facto* control.

# Cellular Resell Agreements

- ◆ All PCS providers should receive equal tariffs (prices, terms and conditions), delivery and quality of service, and distribution and marketing rights for cellular resell.

# Capacity Utilization

- ◆ **No single customer or service reseller can purchase or lease greater than 25% of the Designated Entity's total spectrum capacity within 5 years of license award.**



# Supermajority Rules

- ◆ All Designated Entity Partners need fair Supermajority Rules to protect control and investments.

# Population Limit

*Limit the ownership of each Designated Entity to 25 Million Pops.*

**RESULT:**

- ◆ **More successful Designated Entity Winners.**
- ◆ **Prevents one well financed Designated Entity from winning all top 98 BTA Markets.**

# **Additional Small Business Financial Support**

- ◆ **Expand enhanced payment terms (10 year T-Bill rate) to small business**